

VZCZCXRO8906

RR RUEHAO RUEHCD RUEHGA RUEHGD RUEHHA RUEHHO RUEHMC RUEHMT RUEHNG  
RUEHNL RUEHQU RUEHRD RUEHRG RUEHRS RUEHTM RUEHVC  
DE RUEHPE #0062/01 0161306  
ZNY CCCCC ZZH  
R 161306Z JAN 09  
FM AMEMBASSY LIMA  
TO RUEHWH/WESTERN HEMISPHERIC AFFAIRS DIPL POSTS  
RHEHAAA/NATIONAL SECURITY COUNCIL WASHINGTON DC  
RUEHC/DEPT OF INTERIOR WASHINGTON DC  
RUEATRS/DEPT OF TREASURY WASHINGTON DC  
RUCPDO/DEPT OF COMMERCE WASHINGTON DC  
RUEHC/SECSTATE WASHDC 9880

C O N F I D E N T I A L SECTION 01 OF 02 LIMA 000062

SIPDIS

STATE FOR EEB/IFD/OMA, EEB/EPPD AND WHA/AND

E.O. 12958: DECL: 01/15/2019

TAGS: [ECON](#) [EFIN](#) [PE](#)

SUBJECT: FINANCIAL CRISIS SLOWS GROWTH - STIMULUS PACKAGE  
TO FOCUS ON LIMITING POVERTY

REF: A. 08 LIMA 1897

[1](#)B. 08 LIMA 1716

[1](#)C. 08 STATE 134459

Classified By: Ambassador P. Michael McKinley, Reason 1.4(b, d)

[1](#)1. (C) Summary: The global financial crisis has slowed Peru's strong growth. While 2008 closed with growth at over 9%, estimates for 2009 have continued to undergo downward revision to about 5.5%. Peru's dependence on metals exports has resulted in mixed effects. The sharp fall of base metals prices in the second half of 2008 cut export earnings drastically. Nevertheless, the country has benefited from the renewed strength of gold and the relative stability of copper prices at profitable levels. The Lima Stock Market went from being the world's most profitable in 2006 to having the region's worst performance in 2008. Peru's banking sector has not suffered drastically from the crisis. The key future effects may be political. The decline in poverty rates will likely slow, and the marginal sectors of society may be more susceptible to arguments against the liberal economic model. The government is attempting to respond with a \$3.3 billion stimulus package and accelerating diversification of trade relationships. End summary.

[1](#)2. (U) This responds to reftel C request for additional reporting on the effects of the financial crisis.

[1](#)3. (U) As September 2008 began, Peru was enjoying its seventh year of strong growth, with expectations of 10% growth for the year. Per-capita GDP was rising steadily, with 2008 estimates of \$4,610 representing an increase of over \$1,300 from 2006 figures. The poverty rate had dropped steadily from 54% in 2001 to 39% in 2007. Precious and base metals, high-end agricultural products and textiles fueled strong export earnings. In 2007, Peru had its ninth straight year with a positive balance of trade and had built reserves of \$35 billion. Standard and Poor's and Fitch granted Peru investment grade ratings. The only cloud on the horizon was inflation; in the context of such rapid economic expansion, projections were for a 2008 inflation rate of over 6% -- well over targets of 2-3%.

[1](#)4. (U) The international shocks that started in September have naturally had an effect on Peru's economic performance. Growth in 2008 should still exceed 9%, but projections for growth in 2009 have been subject to steady downward revisions, with the latest figures holding at about 5.5% for the coming year. The fall of base metals prices to levels they saw three years ago cut into export earnings, as did the sudden weakening of U.S. demand for Peruvian asparagus and textiles. Peruvian exports to the U.S. still grew, but Peru's trade balance with the U.S. probably registered a

modest deficit in 2008. Some new investments in the mining sector went on hold, and shares of profits that mining companies provide to regional governments have shrunk. The small Lima Stock Market, comprised mostly of mining companies, lost most of the value it had built during a two-year spike, dropping 64% of its value in 2008. This took it from a position as the world's most profitable market to that of being the region's worst performer. The other side of the coin: inflation has dropped and should register 3.5% in 2009. Reduced fuel prices have also decreased costs.

15. (U) Peru has not experienced the severe negative financial effects that have plagued other countries in the region. Banks did not have great exposure to U.S. and European financial markets, and Peruvian financial institutions have not suffered collapses. Peru's mining companies have been in business for many years and were profitable at pre-2005 prices. Therefore, while current base metal prices represent a decline in profits from the heady days of the past three years, earnings still outpace production costs. Peru is a major exporter of gold and silver. The prices of both of these metals are down from spikes in the first half of 2008, but both have recovered strength recently. Gold is liable to benefit from its status as a haven during the global downturn.

16. (C) Peru's problem is less a matter of macro-economic factors than one of addressing the expectations of the sector of society that remains on the margins. If slower growth means that poor people fail to see the improvements that they expect, then those people could become even more susceptible to populist political arguments. As we noted in reftel B, this can have an impact on the political consensus that

LIMA 00000062 002 OF 002

underlies the pragmatic economic policies the past several government have pursued. With a presidential election coming up in 2011, the continuation of the responsible economic policies of the past several years is potentially at stake.

17. (U) Peru has responded with both internal and external policy measures. In December, the government announced a \$3.3 billion stimulus package (reftel A). This amounts to about 2.47% of the country's GDP. In addition to injecting money into the economy, a further goal of the package is to provide direct assistance to the poor. The money comes from off-budget reserve funds. The intention is to start disbursements toward projects in the first quarter of CY 2009, counteracting the seasonal lull in government expenditures. Half the money will go toward infrastructure projects and other government projects that the 2009 budget did not cover. In addition, a billion dollars -- one-third of the new funds -- will go directly to the construction sector. Other areas of emphasis are small and medium enterprises, the export sector, and direct assistance to workers and to the poor.

18. (U) Another policy response is diversification of trade relationships. The U.S. is Peru's largest single source of both imports and exports. With a weakening of the U.S. market, Peru has accelerated moves to expand trade with Europe and Asia through a network of free trade agreements. Together with the bilateral U.S.-Peru agreement, these measures will reduce tariffs and address many non-tariff barriers to trade.

MCKINLEY